

If Internet access service providers provide both transmission and data processing services, the charges for each must be disaggregated and separately identified. See 86 Ill. Adm. Code 495.100. (This is a GIL).

December 19, 2001

Dear Xxxxx:

This letter is in response to your letter dated October 4, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

AAA, a telecommunications company, hereby requests a letter ruling or advisory opinion regarding the taxability of various Internet service offerings in the State of Illinois.

AAA currently offers or plans to offer Dedicated Internet Access services to business customers in the State of Illinois. The pricing components for AAA Dedicated Internet Access service are as follows:

- Dedicated Access Charges
- IP Port Charges
- Customer Premise Equipment Charges
- Managed Service Charges

Charges for Customer Premise Equipment represent charges for the sale or lease of tangible personal property (routers, digital service units, etc.) necessary to the provision of the service. Charges for Managed Services represent charges for the maintenance of related equipment and other support services. AAA does not seek an opinion regarding these price elements. The purpose of this inquiry is to ascertain the taxability of dedicated access charges and IP port charges.

The dedicated access charges represent the cost of connectivity between the customer premise and the nearest AAA Point-of-Presence. This scalable access is not shared by other customers, and allows the customer to have 'always available' connectivity with AAA's internet backbone.

AAA assesses several distinct charges to recover the cost of providing the access and cabling necessary to provide a dedicated circuit between the customer and the IP port at the AAA Internet Node. Please note that these components may vary based on the customer situation and the port speed selected. In addition, one or more of the coordination or connection fees may be waived in certain promotions. However, at least one of the following cost elements, representative of the cost of providing a dedicated circuit between the customer and AAA's internet backbone, will be present.

-Access Line or Local Loop: These monthly charges are for the local loop between the customer's premises and the nearest AAA Point-of-Presence (POP). Exact pricing will vary based on access speed and the customer's NPA-NXX. Please note that no specific fee is charged for transport from the AAA POP to the nearest AAA Internet Node site.

-Access Coordination Fee (ACF): This amount is assessed per circuit as a monthly recurring charge when a customer appoints AAA as the single point of contact for the customer's service. It is used to recoup the cost of designing and testing a circuit, generating and issuing access service requests, and trouble resolution.

-Central or Control Office Connection (COC): This amount is assessed per circuit as a monthly recurring charge, and is designed to recover the costs associated with digital cross connection at the AAA Point-of-Presence.

-Entrance Facility Charge (EFC): This fee is assessed by AAA to recover costs incurred when using a leased facility to bring a Customer Provided Access circuit into AAA's POP.

As stated above, individual connectivity cost elements are sometimes waived or consolidated into a single charge for access, cabling, and connectivity between the customer premise and the AAA POP.

An IP port is the point of interface between the customer's aforementioned dedicated connection and AAA's internet backbone. It is a physical socket and plug located at AAA's Internet Node Network Edge Router that connects the customer's dedicated circuit to the AAA IP network backbone circuits. Each IP network port is tied to a specific customer and charges for the port are billed to the customer that it represents.

The traffic that flows through the IP port is in the form of Internet Protocol (IP) packets. These packets are essentially encapsulated bits of information that carry data across the various computer networks that make up the Internet, including AAA's internet backbone network. In effect, the IP port is the gateway that allows this information to enter AAA's internet network. These packets can both enter and exit the network through this gateway. Consequently, employees of a AAA Dedicated Internet Access customer have the ability to access the Internet through this service. These employees may also utilize the service to access the customer's corporate Intranet or Local Area Network (LAN), should these networks exist.

The charges for an IP port vary based on bandwidth (capacity to handle the transfer of information at various speeds), the term of the customer contract, and other factors that are specific to each price structure. Currently, there are two price structures in place for Dedicated Internet Access, Flat Rate and Burstable. Both structures have standard term discounts, and there exists within each structure limited ability to add additional

discounts based on the customer's situation. The elements that are unique to each structure are as follows:

-Flat Rate: Flat rate ports are given a fixed monthly charge that varies according to the bandwidth capacity of the port and the contractual term. Discounts may apply based on the length of the term. This price structure will not vary based on customer usage.

-Burstable: Burstable ports are also priced based on the bandwidth capacity of the port and the term of the contract. As is the case with Flat Rate pricing, discounts may apply based on the length of the term. However, rather than a fixed monthly rate, the monthly charge will vary based on average port utilization. Consequently, the Burstable structure can result in significant monthly bill variation based on fluctuations in customer usage.

It is important to note that any Flat Rate or Burstable Port Dedicated Internet Access customer, with the purchase of each new dedicated port, receives the following services free of additional charge:

- Primary Domain Name service for a maximum of five primary domain names.
- Secondary Domain Name service for a maximum of 50 zones.
- One Internet News Feed, if requested.

In addition to these monthly charges, there is a one-time charge for installation of the IP port. This charge will vary based on port speed and configuration. In some promotions, the installation charges may be waived.

In addition to the aforementioned characteristics, IP ports serve as a gateway for the following applications:

-Non-Transit: Transit is the process of routing IP packets across a single network. Transit service is the standard offering, and is not a separate price element of Dedicated Internet Access. This process enables users to have access to content anywhere on the Internet. However, a customer has the option of purchasing non-transit service. Purchasers of non-transit services only have access to content on AAA's internet backbone.

-Internet Virtual Private Network (IVPN): Internet Virtual Private Networking is the creation of a private network over a public network. IVPN devices use protocols to create virtual 'pipes' or 'tunnels' across a shared network. Private data can be transported through these tunnels and may be encrypted for additional security. IVPN can be used to connect offices, telecommuters, clients, partners, and vendors to the Dedicated Internet Access customer. The IP port merely serves as a gateway for this service, however. All charges associated with the creation of an IVPN, including charges for necessary equipment, security, and network management are separate price elements in addition to the basic IP port charge.

-Value Added Services and other IP Applications: While an IP port enables the Dedicated Access customer to have access to AAA's internet backbone, all other IP related services and applications will have separate price elements. For example, a customer wishing to purchase web hosting service, additional Domain Name support, E-Commerce applications, or any other AAA IP related service will incur additional

charges for the specific desired service. The IP port only acts as a physical and virtual gateway for the data necessary to support these applications.

In summary, the charges for dedicated access represent the costs of connectivity and transport between the customer premise and the AAA POP, while the charge for an IP port represents the charge for the actual physical and virtual interface between the customer's dedicated connection and AAA's internet backbone. While the IP port price structures may differ, the IP Port charge is in consideration for the customer's ability to access AAA's internet backbone and the Internet as a whole. As such, it is a prerequisite for all other separately priced Internet Protocol based offerings. AAA hereby requests guidance on whether the monthly charges for (1) dedicated access and (2) IP ports are subject to the Telecommunications Excise Tax in the following situations:

- A.) AAA Dedicated Internet Access is sold to a business entity. The entity and its employees are the ultimate consumer of the service, utilizing the various components of the service including the IP port to access the Internet for business purposes.
- B.) AAA Dedicated Internet Access is sold to a business entity. The entity and its employees are the ultimate consumers of the service, utilizing the various components of the service including the IP port to access the Internet and corporate Intranet for business purposes.
- C.) AAA Dedicated Internet Access is sold to an Internet Service Provider (ISP). The ISP may or may not consume a small portion of the service, but the bulk of the service, if not the entire portion, is repackaged by the ISP and resold to end users as Internet access.
- D.) AAA Dedicated Internet Access is sold to a foreign telecommunications provider. The foreign telecommunications provider may or may not consume a small portion of the service, but the bulk of the service, if not the entire portion, is repackaged by the foreign telecommunications provider and resold to end users located outside of the United States as Internet access.

Thank you in advance for your assistance. If you have any questions or concerns, or if we have failed to follow the proper procedure to obtain a letter ruling or advisory opinion, please do not hesitate to contact me.

The Telecommunications Excise Tax is imposed upon the act or privilege of originating or receiving intrastate or interstate telecommunications in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers. See 86 Ill. Adm. Code 495, enclosed.

Pursuant to Section 495.100(a), "gross charge" means the amount paid for the act or privilege of originating or receiving telecommunications in this State and for all services and equipment provided in connection therewith by a retailer, valued in money, whether paid in money or otherwise, including cash credits, services and property of every kind or nature, and shall be determined without any deduction on account of the cost of such telecommunications, the cost of material used, labor or service cost or any other expense whatsoever. This includes access charges such as charges for IP

ports. These items are fully included in gross charges subject to the Telecommunications Excise Tax.

Generally, persons that provide subscribers access to the Internet and who do not, as part of that service, charge customers for the line or other transmission charges which are used to obtain access to the Internet, are not considered to be telecommunications retailers. See 86 Ill. Adm. Code 495.100(d).

It is our general understanding that most Internet access providers do not, as part of their billing, charge customers for such line charges, but instead, pay to their telecommunications providers all transmission costs that they incur in providing the service. Generally, the customers pay to their providers all transmission costs that they incur while using the service. The single monthly fee charged by such retailers, which often represents a flat charge for a package of items including Internet access, E-mail, and electronic newsletters would generally not be subject to the Telecommunications Excise Tax.

However, please note that persons providing customers with the Internet access described above, but who also provide customers the use of 1-800 service, and separately assess customers with per minute charges for the use of such 1-800 numbers, are considered to be telecommunications retailers. Such retailers will incur Telecommunications Excise Tax on charges made for such 1-800 services. If, however, such Internet service providers do not separately assess customers with per minute charges, but pay their own providers for all transmission costs for the 1-800 service, they are not considered to be telecommunications retailers.

If Internet access service providers provide both transmission and data processing services, the charges for each must be disaggregated and separately identified. See 86 Ill. Adm. Code 495.100(c), enclosed. The statute does not require disaggregation on the customers' invoice, however. Therefore, it is the Department's position that so long as the non-telecommunications charges are disaggregated from the telecommunications charges in the retailers' books and records, for audit purposes, such disaggregation need not be shown on the customers' invoice. If the non-telecommunications charges are not disaggregated from the telecommunications charges, the full amount will be subject to Telecommunications Excise Tax. If none of the charges billed were for telecommunications, then none of the charges would be subject to tax.

In the context of a General Information Letter, we are unable to rule definitively as to whether the services you provide are subject to Telecommunications Excise Tax. However, the dedicated access charges and the IP Port charges, as described, appear to be charges made for transmission that would be considered telecommunications subject to tax. In this case, tax is assessed based upon the gross charges for the service. If your company sells telecommunications to Internet Service Providers, it can accept certificates for resale if such providers plan on reselling the telecommunications services to their customers. If not, the ISPs would remit tax to you on such charges as explained above.

Effective January 1, 1998, the Telecommunications Municipal Infrastructure Maintenance Fee Act (Act) (35 ILCS 635/1 et seq.) provides for the imposition of various fees upon telecommunications retailers.

Section 15 of the Act imposes a State infrastructure maintenance fee upon telecommunications retailers, as that term is defined in 35 ILCS 635/10, "equal to 0.5% of all gross charges charged by the telecommunications retailer to service addresses in this State for telecommunications, other than wireless telecommunications, originating or received in this State."

(35 ILCS 635/15(b).) Section 15 also provides for an optional infrastructure maintenance fee which telecommunications retailers may pay "with respect to the gross charges charged by the telecommunications retailer to service addresses in a particular municipality for telecommunications, other than wireless telecommunications, originating or received in the municipality...." (35 ILCS 635/15(c).) These fees are collected, enforced and administered by the Illinois Department of Revenue. (35 ILCS 635/25(b))

Section 20 of the Act provides that municipalities may impose a municipal infrastructure maintenance fee upon telecommunications retailers. This fee is based upon gross charges charged by the telecommunications retailers to service addresses in the municipality for telecommunications originating or received in the municipality. This fee is collected, enforced, and administered by the municipality imposing the fee. (35 ILCS 635/25(c).)

Illinois municipalities are also authorized to impose a municipal telecommunications tax. (See 65 ILCS 5/8-11-17.) The tax is imposed on the act or privilege of originating in such municipality or receiving in such municipality intrastate or interstate telecommunications by a person at a rate not to exceed 5% of the gross charges for such telecommunications purchased at retail by such person. (See 65 ILCS 5/8-11-17(a)(1) and 65 ILCS 5/8-11-17(a)(2).) This tax may only be imposed if the municipality does not have in effect an occupation tax imposed on persons engaged in the business of transmitting messages by means of electricity as authorized by Section 8-11-2 (65 ILCS 5/8-11-2) of the Illinois Municipal Code. The municipality imposing the tax provides for its administration and enforcement, not the Illinois Department of Revenue. Therefore, questions regarding this tax should be addressed to the individual municipalities imposing it. There is no equivalent statute for county governments.

In addition, the Emergency Telephone System Act provides that "[t]he corporate authorities of any municipality or any county may, subject to the limitations of subsections (c), (d), and (h), and in addition to any tax levied pursuant to Section 8-11-2 of the Illinois Municipal Code, impose a monthly surcharge on billed subscribers of network connection provided by telecommunication carriers engaged in the business of transmitting messages by means of electricity originating within the corporate limits of the municipality or county imposing the surcharge at a rate per network connection determined in accordance with subsection (c)." (See 50 ILCS 750/15.3(a) and (c).) "The surcharge authorized by this Section shall be collected from the subscriber by the telecommunications carrier providing the subscriber the network connection as a separately stated item on the subscriber's bill." (50 ILCS 750/15.3(f).) This surcharge is paid to the municipality, county or Joint Emergency Telephone System Board. (See 50 ILCS 750/15.3(g).) Questions regarding the surcharge should be addressed to the municipality or county imposing it.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis

Associate Counsel

MAJ:msk
Enc.